

Lessors of tangible personal property under true leases in Illinois are deemed end users of the property to be leased. See 86 Ill. Adm. Code 130.220. (This is a GIL).

February 29, 2000

Dear Xxxxx:

This letter is in response to your letter dated January 31, 2000. The nature of your letter and the information you have provided require that we respond with a General Information Letter, which is designed to provide general information, is not a statement of Department policy and is not binding on the Department. See 2 Ill. Adm. Code 1200.120(b) and (c), enclosed.

In your letter, you have stated and made inquiry as follows:

COMPANY is an equipment lessor that does business in all 50 states. We are requesting a written response regarding the proper treatment for the following transaction with Company B.

COMPANY purchases an aircraft to lease to Company A. The FAA title is in the name of COMPANY. At the end of the long term lease (over 12 months), Company A decides to return the aircraft to COMPANY, rather than exercise their fair market value purchase option. Hence, COMPANY finds an appropriate hangar location and puts the aircraft into inventory. Shortly thereafter, COMPANY rents the airplane to Company B. The rental agreement to Company B is a short term agreement, less than 12 months.

Question 1: What is the proper sales tax treatment for the short term rental agreement with Company B? Does sales/use tax apply upfront on the cost or over the stream on the rental payments? If tax applies upfront, is it based on the original purchase price or depreciated value?

Question 2: If COMPANY paid sales or use tax upfront upon the original purchase for lease to Company A, do we have any obligation to charge sales/use tax to Company B? If we do, are we allowed a credit for the tax already paid (a) when it was paid to your state and (b) when it was paid to another state?

Question 3: If COMPANY purchased the aircraft tax free for resale, and charged sales/use tax over the stream of payments to Company A, do we have any obligation to charge sales/use tax to Company B?

Question 4: Does your state differentiate between a short term rental agreement and a short term lease agreement?

Thank you for your response. If you have any questions, I can be reached at #####.

Please note that the State of Illinois taxes leases differently for Retailers' Occupation Tax and Use Tax purposes than the majority of other states. For Illinois sales tax purposes, there are two types of leasing situations: conditional sales and true leases.

A conditional sale is usually characterized by a nominal or one dollar purchase option at the close of the lease term. Stated otherwise, if lessors are guaranteed at the time of the lease that the leased property will be sold, this transaction is considered to be a conditional sale at the outset of the transaction, thus making all receipts subject to Retailers' Occupation Tax.

A true lease generally has no buy out provision at the close of the lease. If a buy out provision does exist, it must be a fair market value buy out option in order to maintain the character of the true lease. Lessors of tangible personal property under true leases in Illinois are deemed end users of the property to be leased. See the enclosed copy of 86 Ill. Adm. Code 130.220. As end users of tangible personal property located in Illinois, lessors owe Use Tax on their cost price of such property. The State of Illinois imposes no tax on rental receipts. Consequently, lessees incur no tax liability.

The above guidelines are applicable to all true leases of tangible personal property in Illinois except for automobiles leased under terms of one year or less, which are subject to the Automobile Renting Occupation and Use Tax found at 35 ILCS 155/1 et seq.

As stated above, in the case of a true lease, the lessors of the property being used in Illinois would be the parties with Use Tax obligations. The lessors would either pay their suppliers, if their suppliers were registered to collect Use Tax, or would self-assess and remit the tax to the Department. If the lessors already paid taxes in another state with respect to the acquisition of the tangible personal property, they would be exempt from Use Tax to the extent of the amount of such tax properly due and paid in such other state. See 86 Ill. Adm. Code 150.310(a)(3) enclosed.

Under Illinois law, lessors may not "pass through" their tax obligation on to the lessees as taxes. However, lessors and lessees may make private contractual arrangements for a reimbursement of the tax to be paid by the lessees. If lessors and lessees have made private agreements where lessees agree to reimburse lessors for the amount of the tax paid, then lessees are obligated to fulfill the terms of the private contractual agreements.

From the information you provided in your letter, the leasing situations to Company A and Company B are both true lease situations. We are assuming for the purposes of this response that you leased to both Company A and Company B in Illinois and paid the Use Tax up front on the purchase of the aircraft as is required for lessors in Illinois. If you paid the Use Tax at the time of purchase, you do not need to pay tax each time you lease the aircraft.

If you had leased the aircraft to Company A outside of Illinois, you would owe Use Tax when you brought the aircraft into Illinois for lease here to Company B. Illinois does allow a credit for taxes properly paid to another state. Further, Illinois does allow a deduction for reasonable depreciation.

I hope this information is helpful. The Department of Revenue maintains a Web site, which can be accessed at [www.revenue.state.il.us](http://www.revenue.state.il.us). If you have further questions related to the Illinois sales tax laws, please contact the Department's Taxpayer Information Division at (217) 782-3336.

If you are not under audit and you wish to obtain a binding Private Letter Ruling regarding your factual situation, please submit all of the information set out in items 1 through 8 of the enclosed copy of Section 1200.110(b).

Very truly yours,

Melanie A. Jarvis  
Associate Counsel

MAJ:msk  
Enc.